

**KEYSTONE
AREA EDUCATION AGENCY 1**

**INDEPENDENT AUDITOR'S REPORTS
BASIC FINANCIAL STATEMENTS AND
SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS**

JUNE 30, 2011

CONTENTS

OFFICIALS		1
INDEPENDENT AUDITOR'S REPORT		2-3
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)		4-10
BASIC FINANCIAL STATEMENTS	<u>Exhibit</u>	
Government-Wide Financial Statements:		
Statement of Net Assets	A	11-12
Statement of Activities	B	13
Governmental Fund Financial Statements:		
Balance Sheet	C	14
Reconciliation of the Balance Sheet –		
Governmental Funds to the Statement of Net Assets	D	15
Statement of Revenues, Expenditures and Changes in		
Fund Balances – Governmental Funds	E	16
Reconciliation of the Statement of Revenues,		
Expenditures and Changes in Fund Balances –		
Governmental Funds to the Statement of Activities	F	17
Notes to Financial Statements		18-27
REQUIRED SUPPLEMENTARY INFORMATION		
Statement of Revenues, Expenditures/Expenses and		
Changes in Balances – Budget and Actual –		
All Governmental Funds and Proprietary Fund		28
Note to Required Supplementary Information – Budgetary Reporting		29
Schedule of Funding Progress for the Retiree Health Plan		30
OTHER SUPPLEMENTARY INFORMATION	<u>Schedule</u>	
Nonmajor Governmental Funds:		
Combining Balance Sheet	1	31
Combining Statement of Revenues, Expenditures		
and Changes in Fund Balances	2	32
Schedule of Revenues by Source and Expenditures by Function –		
All Governmental Fund Types	3	33
Schedule of Expenditures of Federal Awards	4	34-35

CONTENTS
(Continued)

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS	36-37
---	--------------

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133	38-39
--	--------------

SCHEDULE OF FINDINGS AND QUESTIONED COSTS	40-42
--	--------------

KEYSTONE AREA EDUCATION AGENCY 1

OFFICIALS

<i>NAME</i>	<i>TITLE</i>	<i>TERM EXPIRES</i>
Board of Directors		
Gary Gassett	President	2013
Merle Gaber	Vice President	2013
Francis Peterson	Member	2011
Walter Pregler	Member	2011
Robert Brown	Member	2011
John Ganshirt	Member	2011
Bill Withers	Member	2013
John Perrenoud	Member	2013
Agency		
Gary Stumberg	Administrator	
Patrick Heiderscheit	Director of Administrative Services	
Candace Brockmeyer	Board Secretary	
Audie Baumgartner	Business Manager	Indefinite
	Treasurer	



SCHNURR & COMPANY, LLP
Certified Public Accountants and Consultants

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Keystone Area Education Agency 1
Elkader, Iowa

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Keystone Area Education Agency 1 as of and for the year ended June 30, 2011, which collectively comprise the Agency's basic financial statements listed in the table of contents. These financial statements are the responsibility of Agency officials. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with U. S. generally accepted auditing standards, and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards and provisions require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Keystone Area Education Agency 1 at June 30, 2011, and the respective changes in financial position and cash flows, where applicable, for the year then ended in conformity with U. S. generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued our report dated November 8, 2011, on our consideration of Keystone Area Education Agency 1's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Management's Discussion and Analysis, Budgetary Comparison, and Schedule of Funding Progress for the Retiree Health Plan information on pages 4 through 10 and 28 through 30 are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. We did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Keystone Area Education Agency 1's basic financial statements. We previously audited, in accordance with the standards referred to in the second paragraph of this report, the financial statements for the nine years ended June 30, 2010 (none of which are presented herein) and expressed unqualified opinions on those financial statements. Other supplementary information included in Schedules 1 through 4, including the Schedule of Expenditures of Federal Awards required by U. S. Office of Management and Budget (OMB) Circular A-133, Audits of State, Local Governments, and Non-Profit Organizations, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Schnurr & Company, LLP

Fort Dodge, Iowa
November 8, 2011

KEYSTONE AREA EDUCATION AGENCY 1

MANAGEMENT'S DISCUSSION AND ANALYSIS

Keystone Area Education Agency 1 provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the fiscal year ended June 30, 2011. We encourage readers to consider this information in conjunction with the Agency's financial statements which follow.

2011 FINANCIAL HIGHLIGHTS

General Fund revenues in 2011 (FY11) were \$24,299,739 while General Fund expenditures for FY11 were \$22,145,887. Financing uses for FY11 were \$463,269. This resulted in an increase in the Agency's General Fund balance from \$3,056,876 in FY10 to \$4,747,459 in FY11, a 55 % increase from the prior year.

USING THIS ANNUAL REPORT

The annual report consists of a series of financial statements and other information, as follows:

- Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the agency's financial activities.
- The Government-wide Financial Statements consist of a statement of net assets and a statement of activities. These provide information about the activities of Keystone Area Education Agency as a whole and present an overall view of the Agency's finances.
- The Fund Financial Statements tell how governmental services were financed in the short term as well as what remains for future spending. Fund financial statements report the Agency's operations in more detail than the government-wide statements by providing information about the most significant funds.
- Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements.
- Required Supplementary Information further explains and supports the financial statements with a comparison of the Agency's budget for the year, and Supplementary Information provides detailed information about the non-major funds.

MANAGEMENT'S DISCUSSION AND ANALYSIS

USING THIS ANNUAL REPORT (Continued)

Reporting the Agency as a Whole

Government-wide Financial Statements

The Government-wide statements report information about the Agency as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the Agency's assets and liabilities. All of the current year revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two Government-wide statements report the Agency's net assets and how they have changed. Net assets — the difference between the agency's assets and liabilities — are one way to measure the Agency's financial health or position.

- Over time, increases or decreases in the Agency's net assets are an indicator of whether financial position is improving or deteriorating, respectively.
- To assess the Agency's overall health, additional non-financial factors, such as changes in the Agency's property tax base and the condition of its facilities, need to be considered.

In the Government-wide financial statements, the Agency's activities consist of one category:

- *Governmental activities:* Most of the Agency's basic services are included here, such as regular and special education instruction, student and instructional staff support services, and administration. Local school districts, federal and state aid finance most of these activities.

Fund Financial Statements

The fund financial statements provide detailed information about the Agency's funds, focusing on its most significant or "major" funds—not the Agency as a whole. Funds are accounting devices the Agency uses to keep track of specific sources of funding and spending on particular programs. Some funds are required by state law or by bond covenants. The Agency establishes other funds to control and manage money for particular purposes, such as accounting for major construction projects or to show that it is properly using certain revenues, such as federal grants.

MANAGEMENT'S DISCUSSION AND ANALYSIS

USING THIS ANNUAL REPORT (Continued)

Reporting the Agency as a Whole (Continued)

Fund Financial Statements (continued)

The Agency has one kind of fund:

- Governmental funds account for all of the Agency's basic services. These focus on how cash and other financial assets that can readily be converted to cash flow in and out and the balances left at year-end that are available for spending. Consequently, the governmental fund statements provide a detailed short-term view that helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the Agency's programs. Because this information does not encompass the additional long-term focus of the Government-wide statements, additional information at the bottom of the governmental fund statements explains the relationship or differences between the two statements. The Agency's governmental funds include: 1) the General Fund, 2) the Special Revenue Fund, and 3) the Debt Service Fund.

The governmental funds required financial statements include a balance sheet and a statement of revenues, expenditures and changes in fund balances.

MANAGEMENT'S DISCUSSION AND ANALYSIS

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of financial position. Keystone Area Education Agency's net assets at the end of fiscal year 2011 totaled approximately \$5.85 million. The analysis that follows provides a summary of the Agency's net assets at June 30, 2011 for the governmental activities.

	Condensed Statement			
	Governmental Activities		Business-type Activities	
	2010	2011	2010	2011
Current and other assets	\$ 6,575,004	\$ 7,948,020	\$ -	\$ -
Capital assets	3,968,199	3,694,209	-	-
Total assets	10,543,203	11,642,229	-	-
Long-term obligations	3,213,320	2,617,152	-	-
Other liabilities	3,074,980	3,174,920	-	-
Total liabilities	6,288,300	5,792,072	-	-
Net assets:				
Invested in capital assets, net of related debt	1,102,796	1,173,806	-	-
Restricted	443,148	445,684	-	-
Unrestricted	2,708,959	4,230,667	-	-
Total net assets	\$ 4,254,903	\$ 5,850,157	\$ -	\$ -

of Net Assets

Total Agency		Percentage Change (%)
2010	2011	2010-2011
\$ 6,575,004	\$ 7,948,020	20.9
3,968,199	3,694,209	(6.9)
10,543,203	11,642,229	10.4
3,213,320	2,617,152	(18.6)
3,074,980	3,174,920	3.3
6,288,300	5,792,072	(7.9)
1,102,796	1,173,806	6.4
443,148	445,684	0.6
2,708,959	4,230,667	56.2
\$ 4,254,903	\$ 5,850,157	37.5

MANAGEMENT'S DISCUSSION AND ANALYSIS

GOVERNMENT-WIDE FINANCIAL ANALYSIS (Continued)

The following analysis shows the changes in net assets for the year ended June 30, 2011:

	Changes in			
	Governmental Activities		Business-type Activities	
	2010	2011	2010	2011
Revenues:				
Program revenues:				
Charges for service	\$ 1,350,035	\$ 1,364,534	\$ -	\$ -
Operating grants and contributions	15,576,256	10,704,369	-	-
General revenues:				
Property taxes	6,001,872	6,066,862	-	-
State foundation aid	5,571,838	6,335,047	-	-
Unrestricted investment earnings	61,600	66,534	-	-
Total revenues	28,561,601	24,537,346	-	-
Program expenses:				
Instruction	166,815	254,817	-	-
Student support services	14,497,977	10,353,709	-	-
Instructional staff support services	7,128,770	6,806,897	-	-
General administration	3,003,234	3,014,773	-	-
Business administration	1,439,312	1,401,730	-	-
Plant operations and maintenance	1,035,062	950,999	-	-
Central and other support services	586	847	-	-
Community service operations	94,418	42,587	-	-
Interest on long-term debt	129,654	115,733	-	-
Total expenses	27,495,828	22,942,092	-	-
Increase in net assets	1,065,773	1,595,254	-	-
Net assets beginning of year	3,189,130	4,254,903	-	-
Net assets end of year	\$ 4,254,903	\$ 5,850,157	\$ -	\$ -

Net Assets

Total Agency		Percentage
2010	2011	Change (%)
		2010-2011
\$ 1,350,035	\$ 1,364,534	1.1
15,576,256	10,704,369	(31.3)
6,001,872	6,066,862	1.1
5,571,838	6,335,047	13.7
61,600	66,534	8.0
28,561,601	24,537,346	(14.1)
166,815	254,817	52.8
14,497,977	10,353,709	(28.6)
7,128,770	6,806,897	(4.5)
3,003,234	3,014,773	0.4
1,439,312	1,401,730	(2.6)
1,035,062	950,999	(8.1)
586	847	44.5
94,418	42,587	(54.9)
129,654	115,733	(10.7)
27,495,828	22,942,092	(16.6)
1,065,773	1,595,254	49.7
3,189,130	4,254,903	33.4
\$ 4,254,903	\$ 5,850,157	37.5

MANAGEMENT'S DISCUSSION AND ANALYSIS

GOVERNMENT-WIDE FINANCIAL ANALYSIS (Continued)

Operating grants and contributions from local, state, and federal sources account for 44% of the total revenue. The Agency's expenses primarily relate to instruction and support services, which account for 76% of the total expenses.

Governmental Activities

Revenues for governmental activities were \$24,537,346 and expenses were \$22,942,092.

FINANCIAL ANALYSIS OF THE AGENCY'S FUNDS

As previously noted, Keystone Area Education Agency uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The Agency's governmental funds reported a combined fund balance that increased from \$3,500,024 to \$5,193,143.

Governmental Fund Highlights

In FY'11 the financial position of the Agency continued to improve as a result of the receipt of the final year of American Recovery and Reinvestment Act (ARRA) monies and the 2% allowable growth commitment that was fully funded by the State of Iowa. In addition, careful scrutiny during the hiring process in preparation for FY'12 gave us the opportunity to pare down staff numbers in order to prepare for the continued drop in student enrollment.

ARRA funding sources provided the Agency with approximately \$3.8 million in additional revenue over the past two years. Those monies enabled us to fund several key initiatives in special education that have served us exceptionally well. Through utilization of a one-time 'maintenance of State and local effort' reduction opportunity within special education during FY'10, we were able to free up sufficient State and local dollars to also fund some valuable educational services initiatives as well. Advances in technology have translated into better services for our schools, and, in addition, we have targeted dollars to projects designed to address issues related to student achievement. Of course, the final component of ARRA monies was to maintain the financial solvency of Keystone AEA. Our improved financial strength can be translated into job-related security for staff and the ability to withstand further cuts without putting programs in jeopardy.

Budgetary Highlights

The Agency's Board of Directors annually adopts a budget on a basis consistent with U.S. generally accepted accounting principles. Although the budget document presents functional disbursements by fund, the legal level of control is at the total expenditure level, not at the fund or fund type level. After required public notice and State Board review, the State Board either approves the budget or returns it with comments. Any unapproved budget must be resubmitted to the State Board for final approval. The budget may be amended during the year utilizing procedures prescribed by the State Board. Over the course of the year, the Agency amended its annual operating budget one time to reflect additional revenue and expenditures associated with the additional services needed and provided to the local school districts. A schedule showing the original and final budget amounts compared to the Agency's actual financial activity is included in the required supplementary information section of this report.

MANAGEMENT'S DISCUSSION AND ANALYSIS

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

On June 30, 2011, the Agency had invested approximately \$3.69 million, net of accumulated depreciation, in a broad range of capital assets, including land, building, computers, Media lending library and audio-visual equipment. Keystone Area Education Agency had depreciation expense of \$494,546 in FY11 and total accumulated depreciation of approximately \$6.27 million on June 30, 2011. More detailed information about capital assets is available in Note 3 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The 2011-12 school year is underway and the State AEA system has been issued a significant revenue reduction by the Iowa Legislature and Governor's Office. A \$20 million statewide cut has been legislated for FY'12 and a \$10 million reduction for FY'13. Those reductions were introduced during the Governor's original budget request to the legislature and the request has been supported. For Keystone AEA an approximate reduction of \$1.4 million in revenues will be our share of the across the board cut for next year. The cut will primarily impact special education as that Division is the only one funded by state aid. With that in mind, we project the fund balance for special education to be cut in half.

The economic recession continues nation-wide and signs of recovery are sporadic, at best. The State of Iowa has improved their financial standing and we hope that translates into more consistent support for programs and services. The revenue stream for Keystone AEA will continue to suffer as student numbers in non-urban settings continues to decline. That reduction is a sign of the times and no reason exists to assume the trend will not continue. To balance the impending revenue shortfalls, the Agency needs to continue to be focused on adjusting staffing numbers and related expenses to serve the number of eligible students and schools. The Agency also needs to continue to monitor discretionary spending; however, we cannot allow the purchasing of technology and other goods and services to become so backlogged that we find ourselves in a position where we cannot get caught up.

Of special importance this year will be the results of the Governor's "Blueprint for Educational Reform." That agenda will be unveiled in October and will have to survive any opposition raised by the Legislature, along with any other outside force(s). The Blueprint will include a new evaluation and compensation system for teachers and will focus on raising test scores for all students, particularly narrowing the achievement gap that exists between those students with IEPs and the general student population. The financial impact of the reform agenda is yet to be determined; however, one cannot imagine that the Agency's need for (and reliance on) adequate State funding levels will be any less important as the AEA statewide system becomes involved with "rolling out" and implementing the reform package.

CONTACTING THE AGENCY'S FINANCIAL MANAGEMENT

This financial report is designed to provide the Agency's citizens, taxpayers, customers, investors and creditors with a general overview of the Agency's finances and to demonstrate the Agency's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Business Office of Keystone Area Education Agency, 1400 2nd St N.W., Elkader, Iowa, 52043-9564.

KEYSTONE AREA EDUCATION AGENCY 1

BASIC FINANCIAL STATEMENT

STATEMENT OF NET ASSETS

June 30, 2011

	Governmental Activities	Business-Type Activities	Total
Assets			
Cash	\$ 6,681,785	\$ -	\$ 6,681,785
Receivables:			
Accounts	245,592	-	245,592
Due from other governments	993,885	-	993,885
Inventories	24,955	-	24,955
Prepaid expenses	1,803	-	1,803
Capital assets (net of accumulated depreciation)	3,694,209	-	3,694,209
Total assets	11,642,229	-	11,642,229
Liabilities			
Accounts payable	324,122	-	324,122
Salaries and benefits payable	2,248,545	-	2,248,545
Interest payable	17,608	-	17,608
Deferred revenue:			
Federal	17,271	-	17,271
Miscellaneous	147,331	-	147,331
Long-term liabilities			
Portion due or payable within one year:			
Capital leases	360,000	-	360,000
Early retirement obligation	1,400	-	1,400
Compensated absences	58,643	-	58,643
Portion due or payable after one year:			
Capital leases	2,160,403	-	2,160,403
Compensated absences	195,622	-	195,622
Net OPEB liability	261,127	-	261,127
Total liabilities	5,792,072	-	5,792,072

(Continued on next page)

KEYSTONE AREA EDUCATION AGENCY 1**Exhibit A
(Continued)****STATEMENT OF NET ASSETS
June 30, 2011**

	Governmental Activities	Business-Type Activities	Total
Total Liabilities	\$ 5,792,072	\$ -	\$ 5,792,072
Net Assets			
Invested in capital assets, net of related debt	1,173,806	-	1,173,806
Restricted for:			
Debt service	445,684	-	445,684
Unrestricted	4,230,667	-	4,230,667
Total net assets	5,850,157	-	5,850,157
Total liabilities and net assets	\$ 11,642,229	\$ -	\$ 11,642,229

See Notes to Financial Statements.

KEYSTONE AREA EDUCATION AGENCY 1**STATEMENT OF ACTIVITIES****Year Ended June 30, 2011**

		Program Revenues	
		Charges for	Operating
	Expenses	Services	Grants and
			Contributions
Functions/Programs:			
Governmental Activities:			
Instruction	\$ 254,817	\$ 49,940	\$ 204,496
Student support services	10,353,709	477,270	9,384,017
Instructional staff support services	6,806,897	409,120	1,036,976
General administration	3,014,773	-	-
Business administration	1,401,730	428,204	-
Plant operations and maintenance	950,999	-	-
Central and other support services	847	-	-
Community service operations	42,587	-	78,880
Interest on long-term debt	115,733	-	-
Total	\$ 22,942,092	\$ 1,364,534	\$ 10,704,369

General Revenues:

Property taxes
State foundation aid
Unrestricted investment earnings

Change in net assets

Net assets beginning of year

Net assets end of year

See Notes to Financial Statements.

Net (Expense) Revenue and Changes in Net Assets		
Governmental Activities	Business-Type Activities	Total
\$ (381)	\$ -	\$ (381)
(492,422)	-	(492,422)
(5,360,801)	-	(5,360,801)
(3,014,773)	-	(3,014,773)
(973,526)	-	(973,526)
(950,999)	-	(950,999)
(847)	-	(847)
36,293	-	36,293
(115,733)	-	(115,733)
(10,873,189)	-	(10,873,189)
6,066,862	-	6,066,862
6,335,047	-	6,335,047
66,534	-	66,534
1,595,254	-	1,595,254
4,254,903	-	4,254,903
\$ 5,850,157	\$ -	\$ 5,850,157

BALANCE SHEET - GOVERNMENTAL FUNDS

June 30, 2011

	Nonmajor Governmental		
	General	Funds	Total
Assets			
Cash	\$ 6,183,047	\$ 498,738	\$ 6,681,785
Receivables:			
Accounts	245,592	-	245,592
Due from other governments	993,885	-	993,885
Inventories	24,955	-	24,955
Prepaid expenditures	1,803	-	1,803
Total assets	\$ 7,449,282	\$ 498,738	\$ 7,948,020
Liabilities and Fund Balances			
Accounts payable	\$ 313,412	\$ 10,710	\$ 324,122
Salaries and benefits payable	2,223,809	24,736	2,248,545
Interest payable	-	17,608	17,608
Deferred revenue:			
Federal	17,271	-	17,271
Miscellaneous	147,331	-	147,331
Total liabilities	2,701,823	53,054	2,754,877
Fund balances:			
Nonspendable:			
Inventory	24,955	-	24,955
Prepaid items	1,803	-	1,803
Restricted for:			
Media materials	1,300	-	1,300
Educator quality	96,466	-	96,466
Teacher mentoring and induction	901	-	901
Specific special purposes	-	445,684	445,684
Unrestricted:			
Unassigned	4,622,034	-	4,622,034
Total fund balances	4,747,459	445,684	5,193,143
Total liabilities and fund balances	\$ 7,449,282	\$ 498,738	\$ 7,948,020

See Notes to Financial Statements.

RECONCILIATION OF THE BALANCE SHEET--**GOVERNMENTAL FUNDS TO THE STATEMENT OF NET ASSETS****June 30, 2011**

Total governmental fund balances (page 14)	\$ 5,193,143
---	---------------------

*Amounts reported for governmental activities in the
Statement of Net Assets are different because:*

Capital assets used in governmental activities are not current financial resources and, therefore, are not reported in the funds. The cost of assets is \$9,959,762 and the accumulated depreciation is \$6,265,553.

	3,694,209
--	-----------

Long-term liabilities, including capital leases, compensated absences and other postemployment benefits, are not due and payable in the current period and, therefore, are not reported in the funds.

	(3,037,195)
--	-------------

Net assets of governmental activities (page 12)	\$ 5,850,157
--	---------------------

	<u><u>5,850,157</u></u>
--	-------------------------

See Notes to Financial Statements.

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES -- GOVERNMENTAL FUNDS
Year Ended June 30, 2011**

	Nonmajor Governmental		
	General	Funds	Total
Revenues:			
Local sources	\$ 7,505,889	\$ -	\$ 7,505,889
State sources	7,607,079	237,607	7,844,686
Federal sources	9,186,771	-	9,186,771
Total revenues	24,299,739	237,607	24,537,346
Expenditures:			
Current:			
Instruction	49,940	204,496	254,436
Student support services	10,264,301	-	10,264,301
Instructional staff support services	6,703,409	1,179	6,704,588
General administration	2,984,918	22,302	3,007,220
Business administration	1,447,122	54	1,447,176
Plant operations and maintenance	653,470	9,576	663,046
Central and other support services	847	-	847
Community service operations	41,880	-	41,880
Debt service	-	460,733	460,733
Total expenditures	22,145,887	698,340	22,844,227
Excess (deficiency) of revenues over (under) expenditures	2,153,852	(460,733)	1,693,119
Other financing sources (uses):			
Transfers in	-	463,269	463,269
Transfers out	(463,269)	-	(463,269)
Total financing sources (uses)	(463,269)	463,269	-
Excess of revenues and other financing sources over expenditures and other financing uses	1,690,583	2,536	1,693,119
Fund balances, beginning of year	3,056,876	443,148	3,500,024
Fund balances, end of year	\$ 4,747,459	\$ 445,684	\$ 5,193,143

See Notes to Financial Statements.

**RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES --
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
Year Ended June 30, 2011**

Net change in fund balances - total governmental funds (page 16) **\$ 1,693,119**

***Amounts reported for governmental activities in the
statement of activities are different because:***

Governmental funds report capital outlays as expenditures while governmental activities report depreciation expense to allocate those expenditures over the estimated useful lives of the assets. Depreciation expense exceeded capital outlay in the current year as follows:

Expenditures for capital assets	\$ 292,343	
Depreciation expense	<u>(494,546)</u>	(202,203)

In the Statement of Activities, the loss on the disposition of capital assets is reported, whereas in the governmental funds, the proceeds from the sale increase financial resources	(71,787)
---	----------

Repayment of long-term debt principal is an expenditure in the governmental funds, but reduces long-term liabilities in the statement of net assets and does not affect the statement of activities.	345,000
--	---------

Compensated absence, early retirement, and other postemployment benefit expense reported in the statement of activities does not require the use of current financial resources and, therefore, is not reported as an expenditure in the governmental funds.	<u>(168,875)</u>
--	------------------

Change in net assets of governmental activities (page 13)	<u><u>\$ 1,595,254</u></u>
--	-----------------------------------

See Notes to Financial Statements.

KEYSTONE AREA EDUCATION AGENCY 1

NOTES TO FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

Keystone Area Education Agency 1 is an intermediate school corporation established to identify and serve children who require special education. The Agency also provides media services and education support services. These programs and support services are provided to 24 school districts and private schools in an eight-county area. The Agency is governed by a Board of Directors whose members are elected on a non-partisan basis.

The Agency's financial statements are prepared in conformity with U. S. generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board.

A. Reporting Entity:

For financial reporting purposes, Keystone Area Education Agency 1 has included all funds, organizations, agencies, boards, commissions and authorities. The Agency has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Agency are such that exclusion would cause the Agency's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Agency to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Agency. The Keystone Area Education Agency 1 has no component units which meet the Governmental Accounting Standards Board criteria.

B. Basis of Presentation:

Government-wide financial statements: The Statement of Net Assets and the Statement of Activities report information on all of the activities of the Agency. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The Statement of Net Assets presents the Agency's nonfiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes, and other debt that are attributable to the acquisition, construction, or improvement of those assets.

Restricted net assets result when constraints placed on net asset use are either externally imposed or imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets consist of net assets that do not meet the definition of the two preceding categories. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

NOTES TO FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies (Continued)

B. Basis of Presentation (continued):

Government-wide financial statements (continued): The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function and 2) grants, contributions and interest that are restricted to meeting the operational or capital requirements of a particular function. Unrestricted interest income and other items not properly included among program revenues are reported instead as general revenues.

Fund financial statements: Separate financial statements are provided for governmental and proprietary funds. Major individual governmental funds are reported as separate columns in the fund financial statements. All remaining governmental funds are aggregated and reported as other nonmajor governmental funds.

The Agency reports the following major governmental fund:

The General Fund is the general operating fund of the Agency. All general revenues and other revenues that are not allocated by law or contractual agreement to some other fund are accounted for in this fund. From the fund are paid the general operating expenditures, including instructional, support and other costs.

C. Measurement Focus and Basis of Accounting:

The government-wide financial statements and the proprietary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been satisfied.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Agency considers revenues to be available if they are collected within 60 days after year-end.

Intergovernmental revenues (shared revenues, grants and reimbursements from other governments) and interest associated with the current fiscal period are all considered to be susceptible to accrual. All other revenue items are considered to be measurable and available only when cash is received by the Agency.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, principal and interest on long-term debt, claims and judgments and compensated absences are recognized as expenditures only when payment is due. Capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as other financing sources.

NOTES TO FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies (Continued)

C. Measurement Focus and Basis of Accounting (Continued):

Under the terms of grant agreements, the Agency funds certain programs by a combination of specific cost-reimbursement grants and general revenues. Thus, when program expenses are incurred, there are both restricted and unrestricted net assets available to finance the program. It is the Agency's policy to first apply cost-reimbursement grant resources to such programs and then general revenues.

When an expenditure is incurred in governmental funds which can be paid using either restricted or unrestricted resources, the Agency's policy is to pay the expenditure from restricted fund balance and then from, less-restrictive classifications – committed, assigned, and then unassigned fund balances.

D. Assets, Liabilities and Fund Equity:

Cash: Cash includes amounts in demand deposits, money market funds and certificates of deposit.

Inventories: Inventories are stated at cost using the first-in, first-out method and consist of expendable supplies and materials. The cost of these items is recorded as an expenditure at the time of consumption.

Capital assets: Capital assets are recorded at historical cost. Donated capital assets are recorded at estimated fair market value at the date of donation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Capital assets are defined by the Agency as assets with initial, individual costs in excess of the following thresholds and estimated useful lives in excess of two years.

Land	No lower limit
Buildings	\$ 5,000
Improvements other than buildings	5,000
Furniture and equipment	1,000
Library books	Aggregated annual purchases

Property, furniture and equipment are depreciated using the straight-line method of depreciation over the following useful lives:

<u>Asset Class</u>	<u>Estimated Useful Lives (In Years)</u>
Buildings	25
Improvements other than buildings	20
Furniture and equipment	5-20
Library books	5

Salaries and benefits payable: Payroll and related expenses for teachers with annual contracts corresponding to the current school year, which are payable in July and August, have been accrued as liabilities.

NOTES TO FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies (Continued)

D. Assets, Liabilities and Fund Equity (continued):

Deferred revenue: Deferred revenue represents an excess of cash advances by the funding source over accrued expenditures at year-end.

Compensated absences: Agency employees accumulate a limited amount of earned but unused vacation and sick leave hours for subsequent use or for payment upon termination, death or retirement. A liability has been recorded in the Statement of Net Assets representing the Agency's commitment to fund non-current compensated absences. This liability has been computed based on rates of pay in effect at June 30, 2011. The compensated absences liability attributable to the governmental activities will be paid primarily by the General and Special Revenue Funds.

Long-term liabilities: In the Government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the governmental activities column in the Statement of Net Assets.

Fund balances: In the governmental fund financial statements, fund balances are classified in three manners. Nonspendable fund balances are amounts which cannot be spent because they are in nonspendable form or because they are legally or contractually required to be maintained intact. Restricted fund balances are amounts restricted to specific purposes when constraints placed on the use of the resources are either externally imposed by creditors, grantors, or state or federal laws or are imposed by law through constitutional provisions or enabling legislation. Committed fund balances are amounts which can be used only for specific purposes determined pursuant to constraints formally imposed by the Board of Directors through resolution approved prior to year end. Committed amounts cannot be used for any other purpose unless the Board of Directors removes or changes the specified use by taking the same action it employed to commit these amounts. Unassigned fund balances are amounts not included in other spendable classifications.

Restricted net assets: In the Government-wide Statement of Net Assets, net assets are reported as restricted when constraints placed on net asset use are either externally imposed by creditors, grantors, contributors or laws and regulations of other governments or imposed by law through constitutional provisions or enabling legislation.

Note 2. Cash and Pooled Investment

The Agency's deposits in banks at June 30, 2011 were entirely covered by Federal depository insurance or by the state sinking fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Agency is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Board of Directors; prime eligible bankers' acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

NOTES TO FINANCIAL STATEMENTS

Note 2. Cash and Pooled Investment (Continued)

Interest rate risk. The Agency's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days but the maturities shall be consistent with the needs and use of the Agency.

Note 3. Capital Assets

Capital assets activity for the year ended June 30, 2011 is as follows:

	Balance Beginning of Year	Additions	Deletions	Balance End of Year
Governmental activities:				
Capital assets not being depreciated:				
Land	\$ 343,373	\$ -	\$ -	\$ 343,373
Total capital assets not being depreciated	343,373	-	-	343,373
Capital assets being depreciated:				
Buildings	5,480,987	-	80,328	5,400,659
Improvements other than buildings	93,000	-	-	93,000
Furniture and equipment	809,429	125,424	-	934,853
Library books	3,311,480	166,919	290,522	3,187,877
Total capital assets being depreciated	9,694,896	292,343	370,850	9,616,389
Less accumulated depreciation for:				
Buildings	2,994,867	165,359	37,593	3,122,633
Improvements other than buildings	62,775	4,185	-	66,960
Furniture and equipment	481,313	136,441	-	617,754
Library books and films	2,531,115	188,561	261,470	2,458,206
	6,070,070	494,546	299,063	6,265,553
Total capital asset being depreciated, net	3,624,826	(202,203)	71,787	3,350,836
Governmental activities capital assets, net	\$ 3,968,199	\$ (202,203)	\$ 71,787	\$ 3,694,209

NOTES TO FINANCIAL STATEMENTS

Note 3. Capital Assets (Continued)

Depreciation expense was charged to functions of the Agency as follows:

Governmental activities:	
Student support services	\$ 3,039
Instructional staff support services	196,251
Business administration	52,482
Plant operations and maintenance	<u>242,774</u>
Total governmental activities depreciation expense	<u>\$ 494,546</u>

Note 4. Changes in Long-term Liabilities

A summary of changes in long-term liabilities for the year ended June 30, 2011 is as follows:

	Balance Beginning of Year	Additions	Reductions	Balance End of Year	Due Within One Year
Capital leases	\$ 2,865,403	\$ -	\$ 345,000	\$ 2,520,403	\$ 360,000
Early retirement obligation	20,185	-	18,785	1,400	1,400
Compensated absences	237,235	111,748	94,718	254,265	58,643
Net OPEB liability	90,497	170,630	-	261,127	-
	<u>\$ 3,213,320</u>	<u>\$ 282,378</u>	<u>\$ 458,503</u>	<u>\$ 3,037,195</u>	<u>\$ 420,043</u>

Capital leases: The Agency is obligated under a lease accounted for as a capital lease. Fixed assets under a capital lease included in buildings totaled \$4,687,173 at June 30, 2011. The lease matures May 1, 2017 and requires interest at an interest rate of 4.25%. The following is a schedule of future minimum lease payments required under the capital lease as of June 30, 2011:

Year Ending June 30,	Principal	Interest	Total
2012	\$ 360,000	\$ 95,642	\$ 455,642
2013	310,000	88,523	398,523
2014	325,000	75,242	400,242
2015	335,000	61,323	396,323
2016	355,000	46,873	401,873
2017 and later years	<u>835,403</u>	<u>26,580</u>	<u>861,983</u>
Total	<u>\$ 2,520,403</u>	<u>\$ 394,183</u>	<u>\$ 2,914,586</u>

Payments under the agreement for the year ended June 30, 2011, including interest of \$115,733, totaled \$460,733.

NOTES TO FINANCIAL STATEMENTS

Note 4. Changes in Long-term Liabilities (Continued)

Early retirement obligation: The Agency offered a voluntary early retirement plan to its employees that was discontinued effective June 30, 2006. Eligible employees must have completed at least fifteen years of full-time service to the Agency and must have reached the age of fifty-five on or before June 30 in the calendar year in which early retirement commences. The application for early retirement is subject to approval by the Board of Directors. Early retirement benefits are equal to 20% of the employee's regular contractual salary in effect during the employee's last year of employment, with additional benefits available related to unused sick leave days and health insurance. Early retirement benefits will be paid in four equal installments in January and June in the years following the start of retirement. Health insurance benefits will be paid for up to five consecutive years after retirement or until the employee's 65th birthday, whichever comes first. At June 30, 2011, the Agency has obligations to one participant with a total liability of \$1,400. Actual early retirement expenditures for the year ended June 30, 2011 totaled \$18,785.

Note 5. Operating Leases

The Agency has leases for copiers and other related equipment that have been classified as operating leases and accordingly, all rents are charged to expenditures as incurred. The leases expire on dates ranging from June 2012 through June 2015.

The following is a schedule by year of future minimum rental payments required under operating leases that

Year Ending June 30,	Amount
2012	\$ 108,690
2013	81,047
2014	63,339
2015	2,100
2016	-
Thereafter	-
	<u>\$ 255,176</u>

have initial or remaining noncancelable lease terms in excess of one year as of June 30, 2011.

Total rental expenditures for the year ended June 30, 2011 for all operating leases, except those with terms of a month or less that were not renewed, was \$118,266.

NOTES TO FINANCIAL STATEMENTS

Note 6. Pension and Retirement Benefits

The Agency contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by State statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P. O. Box 9117, Des Moines, Iowa 50306-9117.

Plan members are required to contribute 4.50% of their annual covered salary and the Agency is required to contribute 6.95% of annual covered payroll. Contribution requirements are established by State statute. The Agency's contribution to IPERS for the years ended June 30, 2011, 2010 and 2009 was \$932,208, \$921,532 and \$867,375, respectively, equal to the required contributions for each year.

Note 7. Other Postemployment Benefits (OPEB)

Plan description: The Agency operates a single-employer retiree benefit plan that provides medical and prescription drug benefits for retirees and their spouses. There are 235 active and 33 retired members in the plan. Participants must be age 55 or older at retirement.

The coverage is provided through a fully insured plan with Wellmark. Retirees under age 65 pay the same premium for the coverage as active employees, which results in an implicit rate subsidy and an OPEB liability.

Funding policy: The contribution requirements of plan members are established and may be amended by the Agency. The Agency currently finances the retiree benefit plan on a pay-as-you-go basis.

Annual OPEB cost and net OPEB obligation: The Agency's annual OPEB cost is calculated based on the annual required contribution (ARC) of the Agency, an amount actuarially determined in accordance with GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfounded actuarial liabilities over a period not to exceed 30 years.

The following table shows the components of the Agency's annual OPEB cost for the year ended June 30, 2011, the amount actually contributed to the plan and changes in the Agency's net OPEB obligation:

Annual required contribution	\$ 120,830
Interest on net OPEB obligation	4,673
Other adjustments to ARC	96,412
Annual OPEB cost	<u>221,915</u>
Contributions made	51,285
Increase in net OPEB obligation	<u>170,630</u>
Net OPEB obligation beginning of year	<u>90,497</u>
Net OPEB obligation end of year	<u><u>\$ 261,127</u></u>

For calculation of the net OPEB obligation, the actuary has set the transition day as July 1, 2010. The end of year net OPEB obligation was calculated by the actuary as the cumulative difference between the actuarially determined funding requirements and the actual contributions for the year ended June 30, 2011.

NOTES TO FINANCIAL STATEMENTS

Note 7. Other Postemployment Benefits (OPEB) (Continued)

Annual OPEB cost and net OPEB obligation (continued): For the year ended June 30, 2011, the Agency contributed \$1,045,472 to the plan. Plan members eligible for benefits contributed \$471,456 to the plan.

The Agency's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation as of June 30, 2011 are summarized as follows:

Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost	Net OPEB Obligation
June 30, 2011	\$ 221,915	84.98%	\$ 261,127
June 30, 2010	11,028	12.19	90,497
June 30, 2009	79,469	0.00	79,469

Funded status and funding progress: As of July 1, 2010, the most recent actuarial valuation date for the period July 1, 2010 through June 30, 2011, the actuarial accrued liability was \$1.039 million, with no actuarial value of assets, resulting in an unfunded actuarial accrued liability (UAAL) of \$1.039 million. The covered payroll (annual payroll of active employees covered by the plan) was approximately \$13,533,000, and the ratio of the UAAL to covered payroll was 7.68 %. As of June 30, 2011, there were no trust fund assets.

Actuarial methods and assumptions: Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumption about future employment, mortality and the health care cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Schedule of Funding Progress, presented as Required Supplementary Information in the section following the Notes to Financial Statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the plan as understood by the employer and the plan members and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

As of the July 1, 2010 actuarial valuation date, the frozen entry age actuarial cost method was used. The actuarial assumptions include a 2.50% discount rate based on the Agency's funding policy. The projected annual medical trend rate is 6%.

Mortality rates are from the RP2000 Group Annuity Mortality Table, applied on a gender-specific basis. Annual retirement and termination probabilities were developed from the retirement probabilities from the IPERS Actuarial report as of June 30, 2009 and applying the termination factors used in the IPERS Actuarial Report as of June 30, 2009.

NOTES TO FINANCIAL STATEMENTS

Note 8. Risk Management

The Agency is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Agency assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

KEYSTONE AREA EDUCATION AGENCY 1

REQUIRED SUPPLEMENTARY INFORMATION

KEYSTONE AREA EDUCATION AGENCY 1**STATEMENT OF REVENUES, EXPENDITURES/EXPENSES
AND CHANGES IN BALANCES -- BUDGET AND ACTUAL
ALL GOVERNMENTAL FUNDS AND PROPRIETARY FUND****Required Supplementary Information
Year Ended June 30, 2011**

	Governmental Fund Types Actual	Proprietary Fund Types Actual	Total Actual
Revenues:			
Local sources	\$ 7,505,889	\$ -	\$ 7,505,889
State sources	7,844,686	-	7,844,686
Federal sources:	9,186,771	-	9,186,771
Total revenues	24,537,346	-	24,537,346
Expenditures/Expenses:			
Current:			
Instruction	254,436	-	254,436
Student support services	10,264,301	-	10,264,301
Instructional staff support services	6,704,588	-	6,704,588
General administration	3,007,220	-	3,007,220
Business administration	1,447,176	-	1,447,176
Plant operations and maintenance	663,046	-	663,046
Central and other support services	847	-	847
Community service operations	41,880	-	41,880
Debt service	460,733	-	460,733
Total expenditures/expenses	22,844,227	-	22,844,227
Excess (deficiency) of revenues over (under) expenditures/expenses	1,693,119	-	1,693,119
Balance, beginning of year	3,500,024	-	3,500,024
Balance, end of year	\$ 5,193,143	\$ -	\$ 5,193,143

See accompanying Independent Auditor's Report.

Budget		Final to Actual
Original	Final	Variance - Favorable (Unfavorable)
\$ 7,451,782	\$ 7,433,471	\$ 72,418
8,027,270	7,838,225	6,461
11,803,316	10,246,001	(1,059,230)
27,282,368	25,517,697	(980,351)

241,387	240,334	(14,102)
13,650,823	10,466,765	202,464
7,469,616	6,938,911	234,323
3,222,673	3,127,291	120,071
1,372,978	1,501,699	54,523
916,481	868,598	205,552
1,100	3,125	2,278
54,519	59,897	18,017
460,757	460,757	24
27,390,334	23,667,377	823,150

(107,966)	1,850,320	(157,201)
2,741,173	3,500,024	-
\$ 2,633,207	\$ 5,350,344	\$ (157,201)

KEYSTONE AREA EDUCATION AGENCY 1
June 30, 2011

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION – BUDGETARY REPORTING

This budgetary comparison is presented as Required Supplementary Information in accordance with Governmental Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for the General Fund and each major Special Revenue Fund.

The Agency's Board of Directors annually prepares a budget on a basis consistent with U. S. generally accepted accounting principles. Although the budget document presents functional disbursements by fund, the legal level of control is at the total expenditure/expense level, not by fund. After required public notice and hearing in accordance with the Code of Iowa, the Board submits its budget to the State Board of Education. The State Board reviews the proposed budget and either grants approval or returns it without approval with comments. Any unapproved budget must be resubmitted to the State Board for final approval. The budget may be amended during the year utilizing procedures prescribed by the State Board.

For the year ended June 30, 2011, the Agency's expenditures/expenses did not exceed the approved budget.

KEYSTONE AREA EDUCATION AGENCY 1

Schedule of Funding Progress for the Retiree Health Plan (In Thousands)

Required Supplementary Information

Year Ended June 30,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a)/c)
2009	7/1/2008	\$ -	\$ 1,023	\$ 1,023	0.00%	\$ 13,459	7.60%
2010	7/1/2008	-	1,023	1,023	0.00%	14,047	7.28%
2011	7/1/2010	-	1,039	1,039	0.00%	13,533	7.68%

See Note 7 in the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB Cost and Net OPEB Obligation, funded status and funding progress.

OTHER SUPPLEMENTARY INFORMATION

COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
Year Ended June 30, 2011

		<div>Special Revenue</div> <div>Juvenile</div> <div>Home</div>			<div>Debt Service</div> <div>Total</div>	
Assets						
Cash		\$	35,446	\$	463,292	\$ 498,738
Total assets		\$	35,446	\$	463,292	\$ 498,738
Liabilities and Fund Balances						
Liabilities:						
Accounts payable		\$	10,710	\$	-	\$ 10,710
Interest payable			-		17,608	17,608
Salaries and benefits payable			24,736		-	24,736
Total liabilities			35,446		17,608	53,054
Fund balances:						
Unreserved, undesignated fund balance			-		445,684	445,684
Total liabilities and fund balances		\$	35,446	\$	463,292	\$ 498,738

See Accompanying Independent Auditor's Report.

**COMBINING STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
Year Ended June 30, 2011**

	Special Revenue		
	Juvenile	Debt	Total
	Home	Service	
Revenues:			
State sources	\$ 237,607	\$ -	\$ 237,607
Total revenues	237,607	-	237,607
Expenditures:			
Current:			
Instruction	204,496	-	204,496
Instructional staff support services	1,179	-	1,179
General administration	22,302	-	22,302
Business administration	54	-	54
Plant operations and maintenance	9,576	-	9,576
Debt service	-	460,733	460,733
Total expenditures	237,607	460,733	698,340
Deficiency of revenues (under) expenditures	-	(460,733)	(460,733)
Other financing sources:			
Transfers in	-	463,269	463,269
	-	463,269	463,269
Excess of revenues and other financing sources over expenditures	-	2,536	2,536
Fund balances beginning of year	-	443,148	443,148
Fund balances end of year	\$ -	\$ 445,684	\$ 445,684

See accompanying Independent Auditor's Report.

KEYSTONE AREA EDUCATION AGENCY 1**SCHEDULE OF REVENUES BY SOURCE AND
EXPENDITURES BY FUNCTION****ALL GOVERNMENTAL FUND TYPES****For the Last Ten Years**

	2011	2010	2009	2008
Revenues:				
Local	\$ 7,505,889	\$ 7,418,063	\$ 7,176,257	\$ 7,027,608
State	7,844,686	6,889,970	7,639,313	6,864,814
Federal	9,186,771	14,253,568	9,334,486	8,366,891
Total	\$ 24,537,346	\$ 28,561,601	\$ 24,150,056	\$ 22,259,313
Expenditures				
Instruction	\$ 254,436	\$ 166,251	\$ 254,911	\$ 638,042
Student support services	10,264,301	14,506,428	11,588,519	9,783,157
Instructional staff support services	6,704,588	7,067,820	6,575,140	5,934,985
General administration	3,007,220	2,999,018	2,969,745	2,985,714
Business administration	1,447,176	1,574,380	1,286,058	1,383,903
Plant operations and maintenance	663,046	745,214	757,033	726,456
Central and other support services	847	586	199	625
Community service operations	41,880	94,240	58,770	83,388
Facilities acquisition and construction	-	-	-	-
Debt service	460,733	444,654	432,385	413,950
Total expenditures	\$ 22,844,227	\$ 27,598,591	\$ 23,922,760	\$ 21,950,220

See accompanying Independent Auditor's Report.

Schedule 3

Modified Accrual Basis					
Years Ended June 30,					
2007	2006	2005	2004	2003	2002
\$ 6,699,556	\$ 6,552,694	\$ 6,402,127	\$ 6,135,625	\$ 5,926,165	\$ 5,692,600
5,721,745	5,175,879	4,923,883	4,891,443	5,588,592	5,503,191
8,719,971	8,870,515	8,502,948	7,665,784	6,644,135	5,714,781
\$ 21,141,272	\$ 20,599,088	\$ 19,828,958	\$ 18,692,852	\$ 18,158,892	\$ 16,910,572
\$ 377,243	\$ 294,653	\$ 121,543	\$ 117,248	\$ 94,162	\$ 82,528
9,337,230	9,438,835	9,322,347	8,422,985	7,666,455	11,754,658
5,720,022	5,699,278	5,402,081	5,624,220	5,242,624	3,540,505
2,872,640	3,005,570	2,979,545	2,691,044	2,618,878	621,985
1,294,592	1,192,424	758,353	571,982	476,412	234,492
725,009	671,528	630,566	768,618	565,719	138,345
576	2,421	192,599	296,276	320,905	266,429
87,292	85,828	-	-	-	-
-	127,727	-	-	-	-
462,950	453,513	361,701	345,683	363,047	349,448
\$ 20,877,554	\$ 20,971,777	\$ 19,768,735	\$ 18,838,056	\$ 17,348,202	\$ 16,988,390

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended June 30, 2011

Project Title	CFDA Number	Pass-through Grantor's Number	Expenditures
Indirect:			
U. S. Department of Education:			
Passed-through Iowa Department of Education:			
Special Education Cluster (IDEA):			
Special Education - Grants to States:	84.027		
Parent-Educator Connection - 2010-2011		07401	\$ 78,880
IDEA - Part B 2010-2011		101001	4,661,454
IDEA - Part B - LEA Flow-Through 2010-2011		1KB2-01	1,756,072
			<u>6,496,406</u>
QPPS Verification Site Visits 2010-2011	84.173	029911	<u>6,270</u>
Section 619 Project 2010-2011	84.173	1011619-01	<u>233,971</u>
Secondary Professional Development 2009-2010	84.323	SPDG-01	18,556
Secondary Professional Development 2010-2011	84.323	SPDG-01	12,536
			<u>31,092</u>
Special Education - Grants for Infants and Families:			
IDEA - Part C Project - 2010-2011	84.181	C10-01	<u>241,697</u>
Vocational Ed - Basic Grants to States	84.048A		<u>187,373</u>
Title III - English Language Acquisition - 2009-2010	84.365	ELA 10-0312	11,524
Title III - English Language Acquisition - 2010-2011	84.365	ELA 11-001	11,245
			<u>22,769</u>
Iowa Safe & Supp Sch, Learning Supp. - 2010-2011	84.184		<u>7,490</u>
Enhancing Education Through Technology - 2010-2011	84.318		<u>62,908</u>
ARRA - Special Education Grants to States,			
Recovery Act (Part B Section 611) - 2009-2010	84.391	RKB1	202,887
ARRA - Special Education Grants to States,			
Recovery Act (Part B Section 611) - 2010-2011	84.391	RKB1	1,334,447
			<u>1,537,334</u>

(Continued on next page)

KEYSTONE AREA EDUCATION AGENCY 1

Schedule 4
(Continued)SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended June 30, 2011

Project Title	CFDA Number	Pass-through Grantor's Number	Expenditures
Indirect (Continued):			
U. S. Department of Education:			
Passed-through Iowa Department of Education:			
ARRA - (Part B Section 619) - 2009-2010	84.392	R619-01	\$ 24,005
ARRA - (Part B Section 619) - 2010-2011	84.392	R619-01	110,904
			<u>134,909</u>
ARRA - (Part C) - 2009-2010	84.393	RC-01	62,291
ARRA - (Part C) - 2010-2011	84.393	RC-01	110,674
			<u>172,965</u>
Passed-through an Iowa LEA:			
Title II, Part A - 2009-2010	84.367	Project 4643	645
Title II, Part A - 2010-2011	84.367	Project 4643	15,684
			<u>16,329</u>
Passed-through an AEA:			
ARRA - Ed Tech Online/eCurr. Initiative - 2010-2011	84.386	Project 4023	3,925
Safe and Drug Free Schools - 2007-2008	84.186	Project 4591	22
U. S. Department of Health and Human Services:			
Passed-through Iowa Department of			
Medicaid Reimbursement:			
Medicaid Direct Services, Part B - 2010-2011	93.778		6,288
Medicaid Direct Services, Part C - 2010-2011	93.778		25,023
			<u>31,311</u>
			<u>\$ 9,186,771</u>

Basis of Presentation: The Schedule of Expenditures of Federal Awards includes the federal grant activity of Keystone Area Education Agency 1 and is presented on the modified accrual basis. The information on this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

See accompanying Independent Auditor's Report.

KEYSTONE AREA EDUCATION AGENCY 1

**INDEPENDENT AUDITOR'S REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF THE FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**



SCHNURR & COMPANY, LLP
Certified Public Accountants and Consultants

**INDEPENDENT AUDITOR'S REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF THE FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors
Keystone Area Education Agency 1
Elkader, Iowa

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of Keystone Area Education Agency 1 (the "Agency"), as of and for the year ended June 30, 2011, which collectively comprise the Agency's basic financial statements listed in the table of contents, and have issued our report thereon dated November 8, 2011. We conducted our audit in accordance with U. S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Agency's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of the Agency's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Agency's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance all deficiencies, significant deficiencies or material weaknesses have been identified.

A deficiency in internal control exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of the Agency's financial statements will not be prevented or detected and corrected on a timely basis.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control which is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Comments involving statutory and other legal matters about the Agency's operations for the year ended June 30, 2011 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Agency. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the Agency, and other parties to whom the Agency may report, including federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Keystone Area Education Agency 1 during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Scharr & Company, LLP

Fort Dodge, Iowa
November 8, 2011

KEYSTONE AREA EDUCATION AGENCY 1

**INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE WITH REQUIREMENTS THAT COULD
HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133**



SCHNURR & COMPANY, LLP
Certified Public Accountants and Consultants

**INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE WITH REQUIREMENTS THAT COULD
HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133**

Board of Directors of
Keystone Area Education Agency 1
Elkader, Iowa

Compliance

We have audited the compliance of Keystone Area Education Agency 1 (the "Agency") with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Agency's major federal programs for the year ended June 30, 2011. The Agency's major federal programs are identified in Part 1 of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grant agreements applicable to each of its major federal programs is the responsibility of the Agency's management. Our responsibility is to express an opinion on the Agency's compliance based on our audit.

We conducted our audit of compliance in accordance with U. S. generally accepted auditing standards, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Agency's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Agency's compliance with those requirements.

In our opinion, the Agency complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2011.

Internal Control Over Compliance

The management of the Agency is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grant agreements applicable to federal programs. In planning and performing our audit, we considered the Agency's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, and to test and report on internal control over compliance in accordance with OMB A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Agency's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance all deficiencies, significant deficiencies or material weaknesses have been identified.

A deficiency in the Agency's internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance such that there is a reasonable possibility material noncompliance with a type of compliance requirement of a federal program will not be prevented, detected and corrected on a timely basis.

A significant deficiency in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

The Agency's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we expressed our conclusions on the Agency's responses, we did not audit the Agency's responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the Agency and other parties to whom the Agency may report including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

Schnarr & Company, LLP

Fort Dodge, Iowa
November 8, 2011

KEYSTONE AREA EDUCATION AGENCY 1

Schedule of Findings and Questioned Costs Year Ended June 30, 2011

Part I: Summary of the Independent Auditor's Results

- (a) An unqualified opinion was issued on the financial statements.
- (b) No significant deficiencies in internal control over financial reporting were disclosed.
- (c) The audit did not disclose any noncompliance that is material to the financial statements.
- (d) No significant deficiencies in internal control over major programs were disclosed.
- (e) An unqualified opinion was issued on compliance with requirements applicable to each major program.
- (f) The audit did not disclose any audit findings that are required to be reported in accordance with Office of Management and Budget Circular A-133, Section .510(a).
- (g) The major programs were:

Clustered programs:

CFDA Number 84.027 – Special Education – Grants to States

CFDA Number 84.173 – Special Education – Preschool Grants

CFDA Number 84.181 – Special Education – Part C

CFDA Number 84.391 – ARRA – Special Education Grants to States, Recovery Act

CFDA Number 84.392 – ARRA – Special Education Preschool Grants, Recovery Act

CFDA Number 84.393 – ARRA – Special Education – Part C, Recovery Act

- (h) The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- (i) Keystone Area Education Agency 1 qualified as a low-risk auditee.

Part II: Findings Related to the Financial Statements:

Instances of Non-Compliance:

No matters were reported.

Significant Deficiencies:

No matters were noted.

Schedule of Findings and Questioned Costs (Continued)
Year Ended June 30, 2011

Part III: Findings and Questioned Costs For Federal Awards:

Instances of Non-Compliance:

No matters were reported.

Significant Deficiencies:

No matters were noted.

Part IV: Other Findings Related to Required Statutory Reporting:

- IV-A-11 Budget: Expenditures during the year ended June 30, 2011 did not exceed the amounts budgeted.
- IV-B-11 Questionable Expenditures: No expenditures that we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979 were noted.
- IV-C-11 Travel Expense: No expenditures of Agency money for travel expenses of spouses of Agency officials or employees were noted.
- IV-D-11 Business Transactions: No business transactions between the Agency and Agency officials or employees were noted.
- IV-E-11 Bond Coverage: Surety bond coverage of Agency officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to ensure that coverage is adequate for current operations.
- IV-F-11 Board Minutes: No transactions requiring Board approval were noted which had not been approved.
- IV-G-11 Deposits and Investments: The Agency complied with the provisions of Chapters 12B and 12C of the Code of Iowa.
- IV-H-11 Certified Annual Report: The Certified Annual Report (CAR) was certified timely to the Iowa Department of Education.

Schedule of Findings and Questioned Costs (Continued)
Year Ended June 30, 2011

IV-I-11 Categorical Funding: No instances were noted of categorical funding used to supplant rather than supplement other funds.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the Keystone Area Education Agency 1 during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Schnarr & Company, LLP

Fort Dodge, Iowa
November 8, 2011